The Apple Effect

The importance of local and the user experience for the banking and financial services industry

Financial Services Report 2018

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Preview

For generations, bricks-and-mortar bank branches have been the cornerstones of the financial service industry, serving their surrounding communities. However, as technology continues to evolve and the preferences of a shifting consumer base further permeate the industry, many are left wondering what relevance the local bank branch will continue to have moving forward.

Alternatively, has an opportunity been created for medium-sized financial institutions to differentiate themselves from the industry giants, allowing them to capture the attention of those who feel less engaged with the traditional system of banking?

The following report combines in-depth interviews with executives from a range of financial institutions with recent industry trends to explore what the future holds for the mid-tier banking and financial services industry.

Areas that are specifically addressed include:

- The current financial services landscape
- Changing consumer expectations
- The impact of millennials on the traditional system
- The ‘fintech’ (i.e. financial technology) disruption
- How to differentiate through local digital marketing

Change is happening, and with the ever-changing wants and needs of consumers, businesses are expected to keep abreast of the latest digital, buyer behavior, and technological trends. With up-to-date, relevant information at their fingertips, consumers in the digital era are more powerful than ever, and failing to adapt to the times can quickly make your services and offerings obsolete.

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Executive summary

Consumers today are more powerful and more in control than ever before. The Internet has opened up the entire world for customers, and technology has fundamentally changed consumer behavior, irreversibly so. As a result, customers are expecting personalized products and high-quality services, and these requirements need to be met—customers will no longer settle for mediocre services.

The financial services industry is facing challenges on several fronts: from digital disruption and the rise of technology-based financial services, to customer experiences that are being outpaced by expectations. How should banks respond? Industry experts agree that some of the most critical ingredients in a bank's recipe for success include a mobile strategy, a local strategy, community involvement, and personalized products and services.

Banks' recipe for success

MOBILE STRATEGY

Mobile/digital-first strategies that cater to millennial preferences must be developed

COMMUNITY INVOLVEMENT

Community involvement has become a decisive factor for many consumers

LOCAL STRATEGY

Local branches are still important; a local strategy goes hand-in-hand with the mobile strategy

PERSONALIZATION

Tailoring products and services to the needs and wants of individual customers is essential

Without a mobile strategy, banks will be unable to cater to the needs of consumers of the 21st century. Millennials clearly have an impact on the financial landscape; they no longer want to stick to the "norms" of transacting that are dictated by traditional banking systems. Additionally, convenience, responsiveness, and reliability have become of paramount importance to all generations, and, unless mobile is at the forefront of their strategy, banks will be at risk of losing market share, sooner rather than later.

The same is true for having a local strategy. Local presence, and understanding the local community in which they operate, is proving to be more important than ever for banks. Some experts even believe that a local strategy must be part of the mobile strategy. Moreover, community involvement plays a big role and is sometimes vital for banks.

More and more banking executives believe that a bank's success is dependent on the community's success. Some even believe that customers make decisions based on factors like these: How is this bank helping to improve my community? What does it have to offer?

In addition to the aforementioned challenges that banks are defying, the Apple Effect is a phenomenon that many industry experts we interviewed believe has a direct impact on the banking industry. Innovative companies, like Apple and its store atmosphere, are setting the bar for customer experience and personalization. This, coupled with the fact that the financial services industry is highly regulated, puts pressure on banks to keep up and to innovate, within limits, in order to attract and retain clients.

The bottom line is that consumers expect more from businesses today, and banks need to be proactive in order to provide valuable services to their clients. This report provides expert insight into the financial industry as a whole, consumer behavior and demands, the challenges faced by banks, and the rules for success.

Introduction

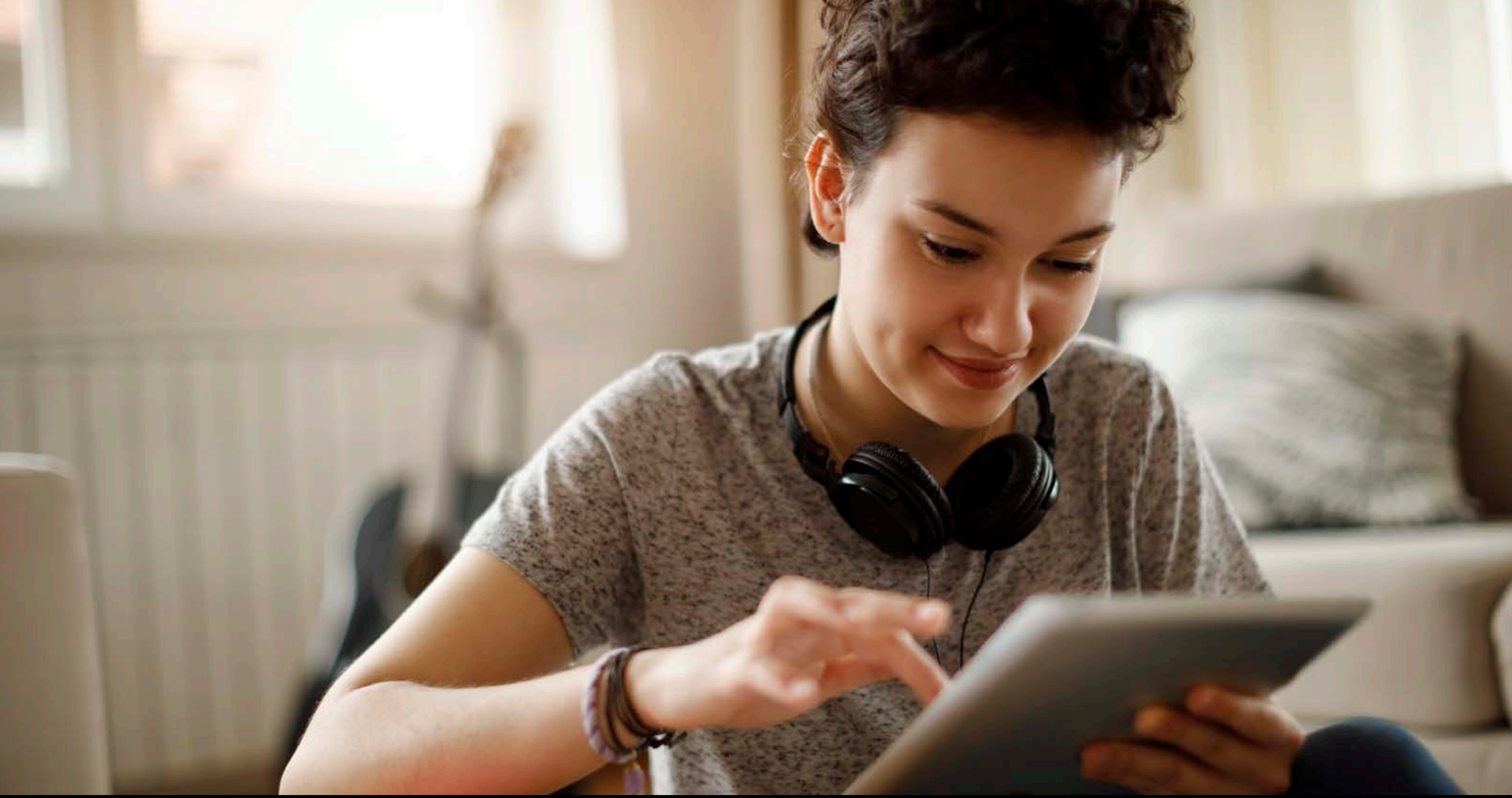
Over the last ten years, two trends have put increased pressure on regional banks and similar financial institutions such as credit unions. First, the biggest national banks in the U.S. have gotten bigger and taken up an increased share of wallet from consumers nationwide. Second, digital and mobile banking products have become ubiquitous with customers in nearly every age bracket, but especially younger generations.

These factors have caused the regional banks in this second tier of size (by assets, number of branches, etc.) to lose the advantage they long had by having a local branch or ATM in the community. But it's exactly this local presence—and knowledge of the communities these banks serve—that can provide the competitive advantage for these regional banks to find new customers and grow their portfolios.

Who we talked to

In an attempt to understand and uncover the challenges facing the financial services industry and what banks can, and should, do to stay relevant, DAC spoke with the following industry experts who shared some of the top industry trends:

- **Tom McEntee,** Chief Marketing Officer at NBT
- **Kelly McNeill-Sproxton,** Director of Member Development at Vancity
- **Nick Necsulescu,** Senior Manager, Digital Marketing and Analytics at President's Choice Financial
- **Lauren Ruff,** Marketing Director at Ixonia Bank

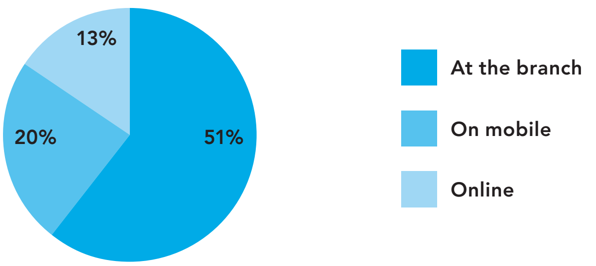


Customer expectations

Consumers' distinct behaviors

Consumers traditionally use digital channels to conduct everyday activities such as paying bills, transferring money or checking balances. But as the task becomes more and more complex, the preferred channel remains visiting a branch to talk to a trusted advisor. For example, in the US, 51% of customers will go to a branch to purchase a financial product vs. 13% on mobile and 20% online.[1] What does this mean for banks?

% of customers by where they purchase financial products



Financial institutions need to ensure that every step of the customer journey is optimized against organizational goals. Innovation is key for attracting and retaining customers—simplifying the user experience can give banks a competitive edge with options like:

- Remote check upload (via phone cameras)
- Mobile payment capabilities
- Seamless navigation across devices

Delivering relevant, local, unique content during the research phase will guide customers from their device, increasing foot traffic at a physical location. This includes local business information, products, and services at a specific branch, and customized experiences.

1. Bain and Company, "Customer Behaviour and Loyalty in Retail Banking," (2015)

"Oh, the times they are a-changin"

Banks need to ensure that their digital capabilities adapt with the changing preferences of their customers. 2015 marked the first time that people preferred online banking vs. visiting a branch.[2] While secondary research shows that all age groups, except for baby boomers, expect some sort of digital functionality from their financial institutions, our interviews with leading experts in the field noted otherwise: while they all indicated that yes, there were differences by generation, multiple sources indicated that this gap is fast closing and they are working to keep pace with this, at times, frenetic change.

The following key features have become table stakes in the financial services industry: easy to use online banking, online bill payments, and online transfers. With an estimated 85 million millennials coming of age over the next few years, the importance of this grows sharply.[3] If financial institutions fail to meet today's consumers' expectations, they risk losing both current and prospective customers.

85 million

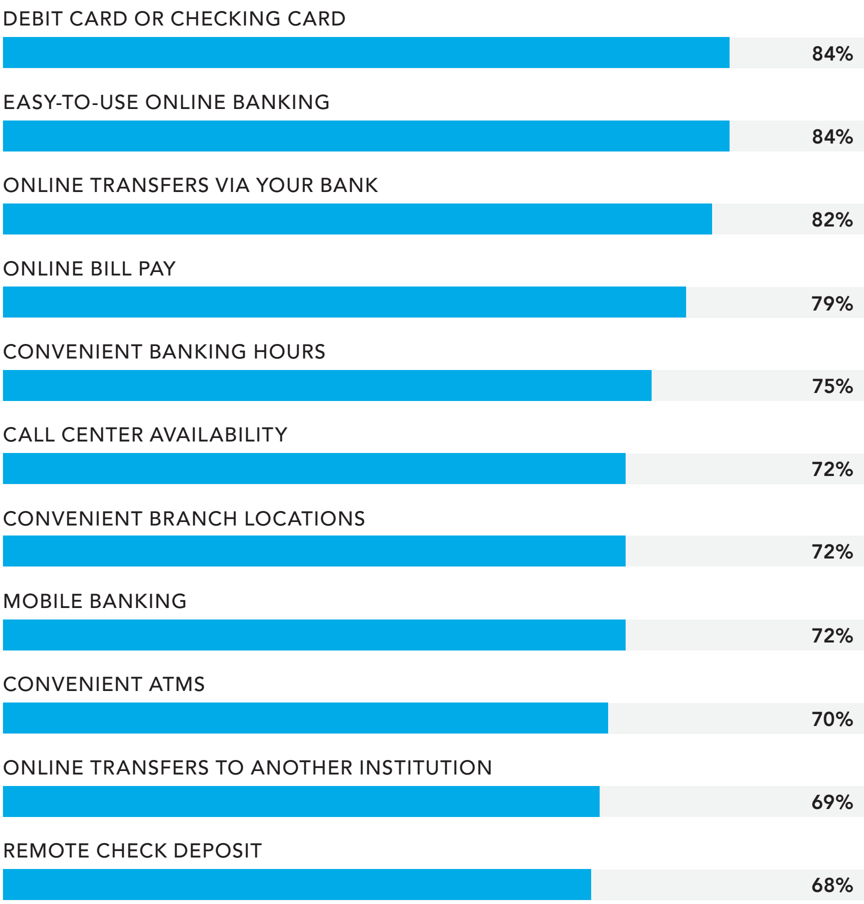
millennials are coming of age in the next few years

2. Javelin Strategy and Research, "2015 Mobile Banking, Smartphone and Tablet Forecast," (2016)
3. McKinsey & Company, "Cutting through the noise around financial technology," (2016)

Embracing mobile banking

Given the pace of technological advancement and the ever-changing demands of consumers, banks must be able to anticipate, adapt to, and capitalize on these rapid changes, in order to meet consumer expectations.

Digital banking channels and features that are excellent/very good according to US internet users, September 2015 (% of respondents)



Note: ages 17+; among those with a checking account

Source: TD Bank Group, "Checking experience Index 2015" conducted by Vision Critical, Oct 12, 2015

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Thanks to digitalization, the "mobile-first" buzzword is becoming more relevant and important to companies across industries. With a mobile-first marketing strategy, the assumption is that the first point of engagement will likely occur on a handheld device.[4] The goal is to leverage the mobile channel to meet customers where they are. Without a mobile strategy, and without engaging with customers and prospective customers on mobile devices, brands will risk losing market share.

> "Brands will win with a mobile strategy."
>
> —**Nick Necsulescu,** Senior Manager, Digital Marketing and Analytics at President's Choice Financial

Nick Necsulescu, Senior Manager, Digital Marketing and Analytics at President's Choice Financial, states that, "The shift to mobile is happening very quickly. The device used is a driver and the ultimate goal regardless of the device/channel is that the customer has a phenomenal experience." He sees that desktops and tablets are quickly being replaced by mobile/on the go devices. "Our consumers and prospects are mobile and we must meet them here. Improving the mobile experience should be at the forefront of the strategy... Brands will win with mobile strategy; you MUST have a mobile channel."

Tom McEntee, CMO at NBT, also stated that he can clearly see a shift to mobile from their data, echoing Necsulescu's views on the subject. McEntee stressed the importance of optimizing the mobile experience and making sure that the mobile sites are user-friendly, and that messaging is consistent across the different digital channels.

4. Vertical Measures, "How to Think Mobile-First for Your Content Marketing Strategy," (2016)

McEntee and Kelly McNeill-Sproxton, Director of Member Development at Vancity, both mentioned that people who have bill pay and online banking are loyal, long-term customers who tend to stay with the financial institution. The findings of a study by J.D. Power on U.S. retail banking may explain why:

> Mobile banking in particular has a direct impact on overall satisfaction, which is 27 points higher among customers who use mobile banking than among those who do not. Among mobile users who are satisfied with the mobile offering (mobile satisfaction score of 800 and above, on a 1,000-point scale) the gap in satisfaction is 197 index points higher than among dissatisfied mobile users, those scoring below 800 index points (868 vs. 671, respectively).[5]

In simple terms, there is a strong correlation between the use of mobile banking and the overall customer satisfaction score: customers who use mobile banking consistently gave their banks higher scores than customers who do not use mobile banking. Moreover, there was a wider gap in overall satisfaction between those who were satisfied with the digital experience and those who weren't relative to those who used the mobile banking service and those who didn't.

5. J.D. Power, "Big Banks Show Significant Gains in Customer Satisfaction as Midsize Banks Decline and Regionals Plateau," (2016)

The impact of millennials

Winning millennial customers

"Having real-time mobile access to personal financial information is a baseline expectation among millennials today."[6] Within these segments, many customers are open to innovative, remote FinTech approaches not offered by traditional banks.[7]

> "Millennials do value the same things [as older generations] just packaged differently.
>
> —**Lauren Ruff,** Marketing Director at Ixonia Bank

Across the board, a common theme was that millennials are setting new expectations in the banking sector. Younger consumers are demanding a relationship with banking institutions built on technology and defined by excellent customer service, more self-service options and financial advice tools. While millennials are driving these expectations, Nick Necsulescu, President's Choice Financial, reports that the "generational differences and [digital] gap is closing quickly." Lauren Ruff, Marketing Director at Ixonia, agrees indicating that she observes that "millennials do value the same things [as older generations], just packaged differently."

75% of millennials are at least somewhat reliant on a mobile banking app to interact with their bank for tasks such as depositing or sending checks, checking their balance, and paying bills.[8]

Based on data collected by Chime in a July 2015 survey of 1,262 millennials, 48% indicated that they prefer using the bank's app on their smartphone. Only 12% indicated that they prefer visiting a branch.

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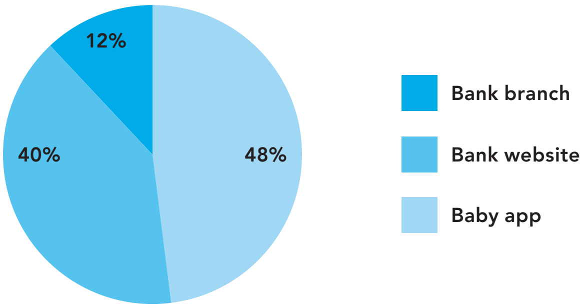
6. eMarketer, "Millennials Embrace Mobile Banking" (2015)
7. McKinsey & Company, "Cutting through the noise around financial technology," (2016)
8. Salesforce, "What Millennials Expect From Their Banks," (2016)

This data suggests that online banking and mobile banking are critical for attracting and retaining the "mobile-first" generation. Delivering an outstanding experience for digital natives is no longer a choice, and banks will need to adapt to this generation's needs and desires by providing convenient, instant, and accessible services.

Preferred banking channel among US millenial internet users, July 2015 (% of respondents)



Note: ages 21–35

Source: Chime, "2015 Millenial Money Mindset Report: The Banking Barometer," Oct 1, 2015

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Nick Necsulescu stated that there are generational differences, but that the gap is closing. "Millennials are bigger users than boomers, but, from 2013 to 2014, 2015, and 2016, more and more boomers are going to mobile."

Millennials expect that banking will, and should, change and serve them differently than it did their parents' generation.[9]

9. American Banker, "What Do Millennials Want from Banks? Everything. Nothing. Whatever" (2016)

What millennials want

MOBILE BANKING

Millennials appreciate flexibility; transacting electronically—anytime, anywhere—is no longer considered a luxury.

ENGAGEMENT

Millennials want to engage with their bank when they need to for advice, feedback on financial decisions, and getting answers to questions.

PERSONALIZATION

Millennials want to form intimate relationships with their banks, and want products and services that are tailored to their needs.

CONVENIENCE

Millennials want real-time information and access to their accounts. They are looking for a smooth and easy experience.

According to Accenture's Banking Shaped by the Customer report, "Millennials switch from their primary bank at a pace nearly double the average of other consumer groups. 18% of millennials switched their primary bank within the past 12 months—compared to 10% of customers 35 to 54 and 3% of people 55 and older."

The report also provides eye-opening statistics that indicate that millennials are making the switch to local institutions:[10]

- Local/community banks are the biggest "winners" in attracting millennials with a 5% migration
- Large regional or national banks are the biggest "losers" with a millennial loss of 16%
- Credit unions experienced a 3% growth in new millennial customers

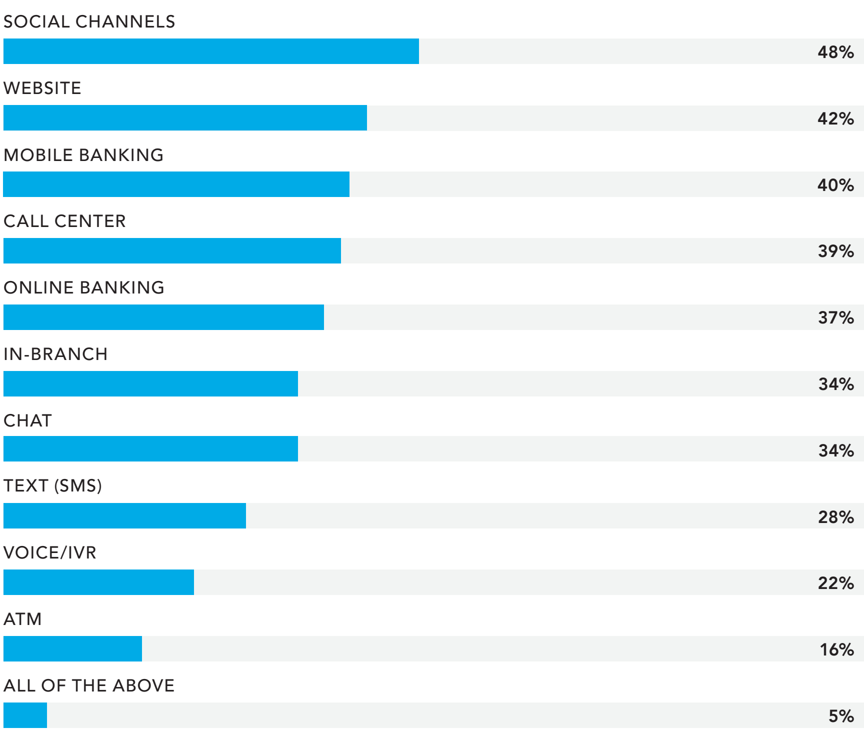
10. Accenture, "Banking Shaped by Customer," (2016)

There is still a long way to go

Studies reveal that, although banking executives are aware of the importance of digital channels, they admit that their efforts can still be improved greatly. TimeTrade's "State of Banking 2015" report shows that four out of the top five areas of improvement are digitally focused (social, websites, mobile and online features). In fact, Accenture recently stated that for the first time.

This is echoed by Lauren Ruff, Marketing Director at Ixonia Bank. Although they don't have a long-term mobile strategy, Ruff said that, as technology advances, they are taking a hard look at it and trying to get ahead of it.

Channels/technologies that are in need of improvement according to US banking executives, July 2015 (% of respondents)



Note: among those whose company uses each channel/technology

Source: TimeTrade, "State of Banking 2015," Sept 15, 2015

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The rise of alternative banking: the FinTech Revolution

A period of stagnant innovation and the recent negative actions of top tier banks has resulted in a decline in trust for the traditional system. This has opened up a window of opportunity for financial tech companies to break into the scene to the tune of $12B in investments in start-ups.[11] The technology has captured the attention of consumers; it is estimated that nearly 40% of consumers have used non-bank providers in the last 12 months.[12] On the surface, business is booming, but upon a closer examination, is this really a threat to banks as we know them?

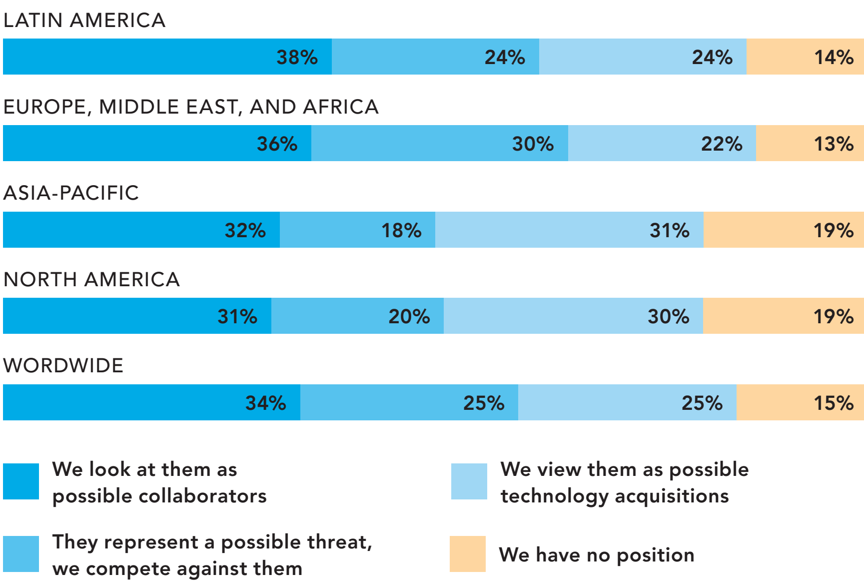
FinTech is a term that is used to describe technology-based financial services. FinTech offers a change of pace from traditional banking. The customer experience is becoming the focal point of the transaction. Additionally, digital solutions are not constrained by operating hours or distance, and there is lower overhead without a physical location or a large workforce, which allows tech companies to offer comparable alternatives at a fraction of the cost. Finally, their solutions are available on platforms that resonate with the shifting population. This may sound like a no-brainer to the discerning customers, but there are also some barriers that are difficult to overcome.

Banks are highly regulated and supported by the government. They have the necessary capital on hand to invest in security, privacy and brand awareness. Their products and services (for the most part) have been tested and perfected over the years. According to industry professionals, and contrary to what many people think, FinTech companies are not as big of a threat as they may seem.

11. Business Insider, "There Is a Massive Void in FinTech: Is Anyone Actually Using This Stuff?," (2016)
12. Ernst & Young, "2016 Consumer Bank Survey," (2016)

The results of the 2016 Worldwide Banking Survey on Digital Transformation, which was conducted by International Data Corporation (IDC), indicated that North American financial institutions do not view FinTech companies as rivals; only 20% of banking executives think that they compete against FinTech companies and that they represent a possible threat to them. A great percentage of banking executives in North America look at FinTech companies as possible collaborators (31%) or as possible technology acquisitions (30%). IDC also believes that banks must work closely with FinTech companies, either by partnering with them or acquiring the capabilities.[13]

Attitude toward financial technology companies among banking executives worldwide, by region, Q2 2016 (% of respondents)



Note: n=503; numbers may not add up to 100% due to rounding

Source: SAP and International Data Corporation (IDC), "The Future Proof Digital Bank," Sep 15, 2016

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13. International Data Corporation, "The Future-Proof Digital Bank," (2016)

Tom McEntee has mentioned that, at NBT, they look for technology with the needs of their customers in mind, and are looking to implement bill pay and P2P (person to person) transfers, where customers can transfer money between accounts without being charged. McEntee also said that they are not implementing these services because disruptors are doing it, but because customers want them. So, while disruptors are leveraging technology to offer services to clients, NBT first conducts research on whether or not its customers would be interested in the new technology/service that is being offered by competitors, and it only offers services that it can fully support.

Lauren Ruff said that, while she is aware of FinTech companies and knows they are out there, she hasn't noticed any disruption. Others, including Nick Necsulescu and Tom McEntee watch the FinTech space—but see these companies as technology players that often get bought out or are looking to partner with financial institutions. As such, FinTech companies move the technology forward, but aren't seen as a disruptive threat currently.

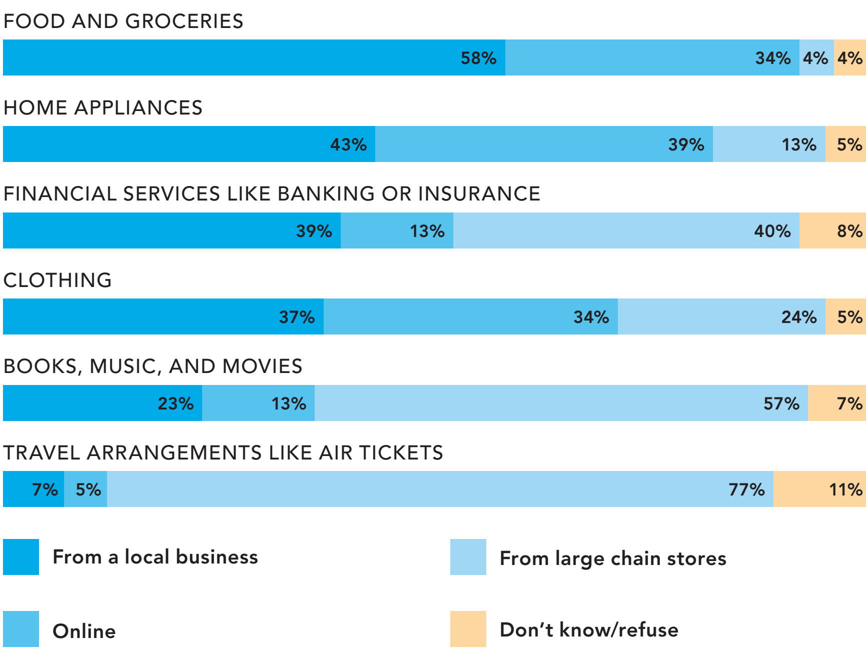
The local digital market

"Local" is king

Providing tailored customer experience to clients has now become a necessity, and local, community banks are becoming increasingly important for consumers. These banks have been striving to gain market share by offering personalized services and great customer experience.

Lauren Ruff believes that local has always been important, and is becoming even more important. "We are always saying that we are local, independent, privately owned… Local means accessibility, flexibility and relationships," explained Ruff. This is echoed by Kelly

Locations where US digital shoppers are most likely to make their purchase, by category, Sep 2015 (% of respondents)



Note: n=759 ages 18+; numbers may not add up to 100% due to rounding

Source: Allstate Corporation and National Journal, "Heartland Poll XXIV," Oct 1, 2015

197905

McNeill-Sproxton, who goes further in stating that, "What is core to Vancity is understanding the local community deeply, so that we can respond to the local issues that arise in the communities we serve." According to eMarketer, although 40% of US digital shoppers purchase financial services online, 39% purchase such services from a local bank.

While mobile is quickly becoming the new standard for banking, Nick Necsulescu believes that local is as important as mobile. "There is a new marketing wave of leveraging data and big data to better understand the moment in time that the consumer is having. This is very important. Their local behavior is a hint, a clue to what they are doing. Pay attention, so that you can capitalize on it. Local is starting to gain momentum and local ads must be a part of a local strategy." Likewise, Kelly McNeill-Sproxton completely dismisses 'mobile' as a stand-alone strategy; she believes that local has to be reflected in the mobile strategy, because local is part of the Vancity brand.

39%

of U.S. shoppers purchase financial services from a local bank

Necsulescu also believes that growth and increasing market share is not easy; banks must provide a very strong incentive for consumers to switch—personalization, mobile, and a great user experience: "Consumers will switch, but must have a great experience. It's not easy to steal market share from the big five."

All of the financial institutions we spoke to have programs in place that are used to understand client preferences. Leveraging this 'big data' will be a key differentiator in creating technologies and solutions that make sense for the consumer. McEntee looks to analytics to understand the different types of engagements consumers have with NBT, and to ensure that the experience and messaging is optimized and consistent across all channels. In looking at the various tiers of banking, McEntee says, "It's about creating stickiness with consumers by offering convenience, security and a sense that NBT is their trusted advisor and financial partner."

> "Local means accessibility, flexibility, and relationships."
>
> —**Lauren Ruff,** Marketing Director at Ixonia Bank

Similarly, Vancity puts a lot of emphasis on its customers (members) and their behavior. "Vancity is an organization that uses and comes at things from a sense of member led innovation. We get close to members to see what works and what's not working," said Kelly McNeill-Sproxton. McNeill-Sproxton explained that their members are at the center of the decisions they make at Vancity. She also mentioned that it is easy for Vancity to put members at the center of their decision-making process because they are smaller, more nimble, local and closer to the communities they serve, relative to other bigger banks.

Community partnerships play a critical role for some financial institutions. Kelly McNeill-Sproxton believes that, "If local businesses thrive, so will the community." McNeill-Sproxton indicated that partnerships are crucial for them and for what they do. Vancity supports the prosperity of small businesses, especially those who help create an economic, social and environmental impact in their local communities. "All generations respond to messages like convenience, security, and local."

McNeill-Sproxton also believes that these partnerships strengthen the community and strengthen Vancity at the same time. It allows them to get close to their members to see what works and what might need to be changed.

Similarly, Tom McEntee is a strong believer in building relationships and getting involved in the community: "Commercial banking is important in these local, small communities, and they want to see their bank involved." McEntee mentioned that consumers will make decisions based on factors like these. He also explained that, while big banks are great with technology, and know how to leverage it to provide a seamless digital experience, they lack the ability to relate to the local consumer.

McEntee stated that NBT's branch managers and tellers are connected to the community and support volunteer efforts. They partner with the community at large in different ways, including supporting schools (which is important for NBT) and getting locally involved with large non-profits, like United Way and the American Cancer Society.

> "If local businesses thrive, so will the community."
>
> —**Kelly McNeill-Sproxton,** Director of Member Development at Vancity

“Consumers’ local behavior is a hint, a clue to what they are doing. Pay attention, so that you can capitalize on it.”

—**Nick Necsulescu,** Senior Manager, Digital Marketing and Analytics at President’s Choice Financial

The “Apple Effect”

Apple’s success is rooted in its exceptional user experience, the way it interacts with its customers, and, of course, its quality products. When it comes to customer service and user experience, Apple has raised the bar for companies across industries—consumers now expect more from the businesses they interact with. Throughout our interviews with key executives, many of their strategies seemed to start with the idea that Apple has changed the game across industries in relation to how consumers interact with brands. This is what our team of researchers refers to as the “Apple Effect”. The ‘iOS’ way of life is driving consumer behavior across all industries, even in the highly regulated banking industry. Those who meet market demands and innovate will win.

Tom McEntee believes that the key lies in connecting the customer journey with the right solution. He understands the implications of the Apple Effect and thinks it’s important to migrate what Apple is doing into the banking industry. NBT has already started doing that; the bank has four digital branches, in an attempt to get the branch to resemble an Apple store as closely as possible. As opposed to a traditional bank, the digital branch has an open area with a “tech bar” in the middle. This set-up allows for a much more interactive, personal connection with the customer, and is designed to support foot traffic.

“Right now, we are focusing on young, higher income areas to convert to these digital branches,” explained McEntee. He also mentioned that using the social aspect to create a banking relationship with the customer is paramount; younger customers want and expect this.

Kelly McNeill-Sproxton also talks about the Apple Effect. She believes that other brands (e.g. Apple) are starting to set customer expectations. Customers now expect personalization, among other things, and this puts pressure on them to keep up. McNeill-Sproxton said that these new expectations force Vancity to select what is right within reason, and to differentiate themselves. This is also increasingly more difficult for banks than it is for other industries because of the regulations that are present: “We have to follow different rules, [which is] another layer of challenge to weigh through,” said McNeill-Sproxton.

Key takeaway

Mobile and localization isn't a trend anymore; it's the new standard.

Operating in the digital world and choosing not to prioritize mobile initiatives could be detrimental to businesses across industries, including banks. Moreover, meeting the needs of local consumers and providing personalized services is now a standard expectation.

As consumer preferences continue to change, and as innovative companies, like Apple, continue to set customer expectations, banks are facing enormous challenges: How do we remain relevant? Are we prepared to improve customer experience in a way that aligns with ever-changing consumer behavior and demands? Do we know who our local consumers are, and are we delivering personalized services to them? How do we leverage FinTech solutions to provide clients with a seamless digital experience? These are some of the questions that executives of mid-tier, regional banks should consider when thinking of how to remain competitive.

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